

HOUSE BILL REPORT

HB 2196

As Reported by House Committee On:
Finance

Title: An act relating to authorizing an expansion of the local option real estate excise tax to fund capital projects in lieu of impact fees.

Brief Description: Providing for expansion of the local option real estate excise tax to fund capital projects.

Brief History:

Committee Activity:

Finance: 3/3/05, 3/7/05 [DPS].

Brief Summary of Substitute Bill

- Authorizes a real estate excise tax (REET) of 0.4 percent for cities and counties to use for certain capital purposes in lieu of imposing and using certain impact fees.
- Authorizes a REET of 0.25 percent for school districts to use for certain school facility capital purposes in lieu of receiving impact fees.
- Preempts the imposition and use of impact fees for: certain purposes, if the 0.4 percent REET is imposed; and purposes relating to school facilities if the 0.25 percent REET is imposed.
- Exempts the sale of certain properties from the REETs.
- Provides that, if a new REET is imposed, an impact fee may not be re-imposed earlier than eight years after the tax is effective.

HOUSE COMMITTEE ON FINANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 5 members: Representatives McIntire, Chair; Hunter, Vice Chair; Conway, Hasegawa and Santos.

Minority Report: Do not pass. Signed by 4 members: Representatives Orcutt, Ranking Minority Member; Roach, Assistant Ranking Minority Member; Ahern and Ericksen.

Staff: Mark Matteson (786-7145).

Background:

Impact fees - Growth Management Act. Counties, cities, and towns that plan under the major provisions of the Growth Management Act (GMA) are authorized to impose impact fees on development activity as part of the financing of public facilities. Impact fees are payments of money required of developers as a condition of development approval and apply to both new development and the expansion of existing development.

The imposition of impact fees is subject to several conditions. Such fees:

1. may be imposed only with respect to certain public facilities that are reasonably related to the impact of the development on the facilities;
2. may not exceed a proportionate share of certain public facilities' costs related to the impact of the development; and
3. must be used for certain public facilities that reasonably benefit the new development.

The public facilities for which the impact fees may be imposed and spent are limited to certain capital facilities that are owned or operated by government entities. These include public streets and roads; publically owned parks, open space, and recreation facilities; school facilities; and fire protection facilities in jurisdictions that are not part of a fire district.

Local ordinances imposing impact fees must include a schedule of fees specific to each type of development activity. The method of fee calculation must take into account the type of development in determining the cost of its anticipated impact. In determining the proportionate share of the fee to be paid by a developer, the formula or method must incorporate:

- the cost of public facilities necessitated by new development;
- an adjustment to the cost of the public facilities for past or future payments made or reasonably anticipated to be made by new development to pay for particular system improvements in the form of user fees, debt service payments, taxes, or other payments earmarked for or proratable to the particular system improvement;
- the availability of other means of funding public facility improvements;
- the cost of existing public facilities improvements; and
- the methods by which public facilities improvements were financed.

Impact fees are required to be used for a permissible purpose within six years of receipt. If not used at the end of the six-year period, the fees must be refunded to the person who paid the fees.

Mitigation fees - State Environmental Policy Act. The State Environmental Policy Act (SEPA) requires every governmental agency to review its proposed major actions and determine if a probable significant adverse environmental impact will arise from the proposed action.

The review process involves a number of potential steps that could result in the preparation of an environmental impact statement for a proposed governmental action. However, very few

proposed governmental actions result in the preparation of an environmental impact statement. Many actions are categorically exempted from the analysis. Proposed actions may be modified or actions may be taken to remove the probable significant adverse environmental impact. The action taken may include the payment of fees to compensate for the adverse impact. The SEPA analysis must consider any and all mitigation measures to determine if, after modification or after the mitigation measures have been taken, a probable significant adverse impact still would arise.

The SEPA analysis reviews a variety of subjects, including the probable impact of a governmental decision on public facilities.

Real estate excise tax. The real estate excise tax (REET) is imposed on each sale of real property, which includes both the transfer of ownership and the transfer of controlling interests. Real property includes any interest in land or anything affixed to land. The state tax rate is 1.28 percent. Additional local rates are allowed. The combined state and local rate in most areas is 1.78 percent or less. The highest rate is 2.78 percent in the City of Friday Harbor. Administration of the tax is both at the county and state levels. County treasurers are designated as agents of the state, cities, and counties in processing the REET.

The Growth Management Act includes a modification to the original 0.25 percent REET authority enacted for local governments and an additional 0.25 percent REET authority for the purposes of providing assistance to local governments required to or choosing to plan under the GMA. The changes mean that local governments subject to GMA requirements can impose taxes of up to 0.5 percent and that the proceeds must be used to finance capital projects identified in a capital facilities plan element of a comprehensive plan.

The GMA-related REET authority specifies that the use of the funds are limited to the planning, acquisition, construction, reconstruction, repair, replacement, rehabilitation, or improvement of certain types of projects:

<u>First 0.25% REET [RCW 82.46.010 (2)*]</u>	<u>Second 0.25% REET [RCW 82.46.035(2)]</u>
Streets	Streets
Roads	Roads
Highways	Highways
Sidewalks	Sidewalks
Street and road lighting systems	Street and road lighting systems
Traffic signals	Traffic signals
Bridges	Bridges
Domestic water systems	Domestic water systems
Storm and sanitary sewer systems	Storm and sanitary sewer systems

Parks

Parks (but not acquisition or replacement)

Recreational facilities

Law enforcement facilities

Fire protection facilities

Trails

Libraries

Administrative / judicial facilities

River / waterway flood control

(* Applies to jurisdictions of over 5,000 persons that plan under GMA)

The modification to the original 0.25 percent REET authority did not affect jurisdictions not planning under the GMA but who were eligible to impose the REET. There are 267 cities and 37 counties that impose the first 0.25 percent REET and 127 cities and 14 counties that impose the second 0.25 percent REET added under the GMA.

Summary of Substitute Bill:

New authority is provided to cities, counties, and school districts to impose a local real estate excise tax (REET) in lieu of certain impact fees. Impact fees are defined as the impact fees authorized for jurisdictions planning under the GMA. Impact fees are also defined as fees authorized under SEPA for the same system improvements that the GMA impact fees are authorized.

City and County - new 0.4 percent REET. Cities and counties may impose a 0.4 percent REET. Proceeds must be used for:

1. the same purposes for which cities and counties that plan under GMA may impose impact fees, but also for fire protection facilities in fire protection districts;
2. the same purposes for which the first 0.25 percent REET may be imposed by cities and counties, but excluding trails, libraries, admin/judicial facilities, and flood control projects; and
3. low-income housing.

A city or county is prohibited from imposing the new REET unless the city or county discontinues impact fees as defined in the bill, other than impact fees relating to school facilities.

Exemptions from the new REET are provided for sales of low-income housing; for sales of timber, agricultural land, and open space properties subject to classification in a current use property valuation program; and the first sale after a tax is imposed of residences that are part

of a new development where impact fee amounts were required before the tax went into effect.

A city or county may not impose an impact fee for streets and roads; parks, open space, and recreation facilities; or fire protection facilities; if the city or county is imposing the new REET. A city or county that imposes the new REET may not re-impose any discontinued impact fees earlier than eight years following the effective date of the REET.

School districts - new 0.25 percent REET. School districts are authorized to impose a 0.25 percent REET. Proceeds must be used for the same purposes that GMA impact fees may be used with respect to system improvements associated with school facilities within the district.

School districts are prohibited from imposing the tax if the city or county in which the district is located is imposing a school impact fee for the school district.

Exemptions from the school district REET are provided for the same sales as in the exemptions from the 0.4 percent REET for cities and counties. In addition, all non-residential property sales are exempt.

If a school district is imposing the new REET, a city or county may not impose an impact fee for system improvements for school facilities within the district. A city or county within which a school district is located may not re-impose any discontinued impact fees with respect to school facilities in the district earlier than eight years following the effective date of the REET imposed by the district.

Other requirements. The GMA impact fee requirements are modified to allow cities and counties to retain unspent impact fees when a REET is imposed under this act if: the fees are spent on qualifying purposes within the six year time frame; and an exemption from the REET is allowed on the first sale of each property within the development that generated the unspent fees.

To administer the new REET for school districts, the county treasurer is designated as an agent of school districts. Other administrative modifications with respect to the new school district authority.

The Office of the Superintendent of Public Instruction (OSPI) is required to develop rules to require school districts to separately report data on impact fees and taxes, by type of source.

Any new tax is effective no sooner than January 1, 2006.

Substitute Bill Compared to Original Bill:

Adds substantive provisions concerning new real estate excise tax authority and preemptive provisions with respect to impact fees.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date of Substitute Bill: The bill takes effect 90 days after adjournment of session in which bill is passed.

Testimony For: This is a much larger issue that I first imagined. Currently, impact fees are one of the only ways for local governments to fund infrastructure. There is nothing much else in the tool box. We are looking at how growth pays for growth. This is a work in progress.

The builders do not like impact fees. Costs are increasing. Affordable housing has suffered. These fees unfairly target seniors and young families seeking to get into the market for the first time. On a \$150,000 home, these average \$6,000. Moving to a real estate excise tax is less regressive, broader based, and is a local option. While we are not for impact fees or a tax, we feel like the REET would be a better source of funding.

For those of us that represent affordable housing interests, impact fees seem like an inefficient expenditure of housing trust fund dollars. We recognize the need for infrastructure and are supportive of this legislation.

Habitat for Humanity builds houses for families that are typically at 25 to 50 percent of the median income in the area. On a house that costs \$70,000 to build, impact fees represent about 7 percent of costs. We would like a mandatory exemption for low-income housing. We would like funds to be used not just for low-income housing debt repayment but for construction as well.

I am a city manager and have listened to both sides of this issue for many years. If I buy the argument that growth should pay for growth, then I must decide whether this payment should be up front or later. I think the back end is better. Impact fees cause hardship when there's not much equity. The home buyer has scraped together a downpayment. It adds to the developer costs, which adds to their interests costs, compounding things. The better way is to pay it out over time, when equity has been built up. REET is less regressive. Our city was largely built out before impact fees were put into place. This would help us rebuild and expand.

(Concerns) Our school board's fear is that we would not be able to recover impact fees once REET is imposed. We're worried that cities and counties would repeal their statutes. We understand that it is an option, but fear that the repeal would occur and then would be difficult to reinstate. Our school does not qualify for a state match. We need impact fees in our school districts and don't want to lose that source.

Testimony Against: We are opposed to impact fees, support the goal of addressing infrastructure, but believe that this is the wrong approach. This takes a huge equity from families on home sales. We need to remember that not all sales are by choice, and this will really dig into any equity that has been built up. Second, this is a tax shift. While impact fees are onerous, they are paid by the wealthier families who can afford new construction. Blue collar families may not be able to afford new construction, and they will in part bear the burden of this tax. There is no nexus here - REET may be used anywhere, not just on new

construction. Washington has the second highest REET in the nation. This is an 80 percent tax increase for cities and counties. This will further reduce home ownership. There is a lot of talk about sin taxes. We don't understand when the realization of the American dream of home ownership became a sin.

This is supposedly a broad-based tax, but only 10 percent of homes are being asked to pay for the new infrastructure. We risk killing the goose that laid the golden egg. In the last quarter of last year, Freddie Mac reported that \$139 billion was taken out of home equity in their portfolio alone. This is money that's fueling a retail economy that is otherwise judged to be weak. The seller does not pay with the price of their home, it must come out of equity. Inventories are also shrinking, down to 85 percent of last year's.

In Whatcom County, we've had a 29 percent increase in median price in the last 12 months, and there has been a 10 percent increase in volume. There are already more REET revenues. This is not a stable tax. We do not want to base our children's income on an unstable tax. I represent a senior citizen who will have to pay an additional \$1,500 if this goes through.

This is a grossly unfair bill to those both in difficult circumstances and early buyers of homes, who have no equity. It will prevent them from entering the market.

As a broad-based tax, a large portion of proceeds will be returned to areas that least need it for growth. Real estate market does not always go up. In addition, sometimes sales are for emergencies. We do not want to see capital projects funded by a volatile source.

We support trying to find more money for infrastructure, and feel that impact fees are the best way to go about this. We are concerned about the provisions in the bill. We are concerned about the open flexibility. Would like to see some smart spending criteria to focus REET and would like to work with the sponsor and the chair in adding language that would allow the tax to vary where costs of growth vary. We would like to see SEPA authority retained for non-affected projects.

Persons Testifying: (In support) Representative Clibborn, prime sponsor; Jeff Hansell, Vice President, Building Association of Washington; Randy Sundberg, Sundberg Construction; Paul Percell, Beacon Development Group; Maureen Howard, Habitat for Humanity of Washington; and Bob Jean, Manager, City of University Place,

(In support with concerns) Genesee Adkins, Futurewise.

(Opposed) Sam Pace and Mike Flynn, Washington Association of Realtors; Richard Baila and Jon Soine, Whatcom County Association of Realtors; Connie Fletcher, Issaquah School Board; George McGilliard, Tacoma-Pierce County Association of Realtors; Joseph Mosolino, Oak Harbor-Whidbey Island Association of Realtors; and Shelia Davies, North Puget Sound Association of Realtors.

Persons Signed In To Testify But Not Testifying: (In support) Paul Parker, Washington Association of Counties; Doug Levy, Cities of Everett, Kent, Federal Way, and Puyallup; David Foster, City of Seattle; Rick Slunaker, Associated General Contractors; Sharon Wylie,

Clark County; and Dave Williams and Alex Pietsh, Association of Washington Cities and City of Renton.

(In support with concerns) Greg Hanon National Association of Industrial and Office Proprietors.

(Concerns) Tom McBride, Association of Washington Businesses; T. K. Bentler, Funeral Directors Association; and Marcia Fromhold, Clark County School Districts.

(Opposed) Dennis Cavalier, Olympia-Thurston County Association of Realtors; Catherine Rudolph and Pat Maddock Tacoma-Pierce County Association of Realtors; and Denise Stiffarm, King and Pierce County School Coalitions.